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FM AMEMBASSY NEW DELHI

TO RUEHC/SECSTATE WASHDC 6971

INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE

RUCPDOC/DEPT OF COMMERCE WASHDC

RHEBAAA/DEPT OF ENERGY WASHDC

RUEATRS/DEPT OF TREASURY WASHDC

RULSDMK/DEPT OF TRANSPORTATION WASHDC

RHMCSUU/FAA NATIONAL HQ WASHINGTON DC

RUEHRC/DEPT OF AGRICULTURE WASHDC

UNCLAS SECTION 01 OF 04 NEW DELHI 001222

SENSITIVE

SIPDIS

STATE FOR SCA/INS AND EEB

USDOC FOR ITA/MAC/OSA/LDROKER/ASTERN/KRUDD

DEPT OF ENERGY FOR A/S KHARBERT, TCUTLER, CZAMUDA, RLUHAR

DEPT PASS TO USTR CLILIENFELD/AADLER/CHINCKLEY

DEPT PASS TO TREASURY FOR OFFICE OF SOUTH ASIA MNUGENT

TREASURY PASS TO FRB SAN FRANCISCO/TERESA CURRAN

USDA PASS FAS/OCRA/RADLER/BEAN/FERUS

EEB/CIP DAS GROSS, FSAAED, MSELINGER

E.O. 12958: N/A

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BEXP, KBIO, KIPR, KWMN, IN

SUBJECT: New Delhi Weekly Econ Office Highlights for the Week of June 8 to June 12, 2009

¶11. (U) Below is a compilation of economic highlights from Embassy New Delhi for the week of June 8-12, 2009, including the following:

-- MOF Preparing for Budget Session
-- Indian Commerce Minister Meets with USTR, Others on WTO
-- Tax Concessions Proposed for Broadcast & Film Industry
-- Will Govt Give Bailout for Air India's Mounting Losses
-- IT Industry Threatens Retaliation If US Tax Breaks Are Withdrawn
-- Chennai Breaks Ground on Metro Rail Project
-- Local Distiller to Produce Smirnoff in Tamil Nadu

MoF Preparing for Budget Session

¶12. (SBU) In a meeting on June 11, Ministry of Finance Joint Secretary (Capital Markets) KP Krishnan told Emboffs and visiting Deputy Assistant USTR for South Asia Claudio Lilienfeld about the preparations underway in his Ministry for the upcoming Budget Session of Parliament next month. Krishnan noted that the prebudget "number crunching" had been done. While the Prime Minister was aware of the fiscal deficit, which acted as a constraint on spending, he also felt challenged to deliver on the social promises made by the government. The media has been correctly characterizing the budget, Krishnan stated, as a vehicle for signaling policy intent and announcing policy changes. He indicated that only the last stage of the budget proposal process was left - the Finance Minister meeting with the Prime Minister. Krishnan described the Finance Minister, based on their meetings together, as someone who is not concerned with minutiae but wants to focus on policy goals and the political issues surrounding change in order to address the political hurdles.

¶13. (SBU) Krishnan then spoke more broadly about the policy review efforts underway across the government. The Joint Secretary stated that the Prime Minister had tasked ministries back in February to identify "unfinished business" that needed completing. He said the PM wanted it done before elections so that, if they won, the UPA could hit the ground running. If they lost, the PM reportedly said the plans would be left as suggestions for the new Prime Minister. That way, the policy reviews done from February to May were either going to be the PM's own plan or his legacy. Krishnan told Emboffs that the Prime Minister had decided to chair three cabinet

committees himself in the new government, as priority areas where he wanted to ensure progress: Human Resource Development, Infrastructure, and Financial Services. Krishnan said that the Prime Minister had also tasked several ministries with drafting legislation to be introduced in the July session with the goal of trying to pass some of the legislation before the session ended sometime in August. (Comment: A very ambitious timeline for Indian legislation. End comment.) Ministries are being pushed because of the government's view that it must accomplish its policy goals in the first two years, ideally this year or next.

¶4. (SBU) Krishnan himself had been tasked with rewriting the pension reform bill (the PFRDA Act), as old age income security was a high priority of the Prime Minister, which he sees as a key part of inclusive growth. The bill would, among other things, consolidate into the New Pension Scheme (NPS) disparate existing pension schemes for workers in different sectors, like handlooms, cigarette rollers, and plantations. He said the Finance Minister was trying to keep an FDI provision out of the legislation, since any future changes would then require additional legislation. They are not wed to any FDI cap in general, Krishnan acknowledged, but the Finance Minister is aware of the time and energy it took to move on the insurance bill amendment raising the FDI cap from 26 to 49%, since he chaired the Group of Ministers on the issue, and has signaled his intent to keep FDI issues out of the legislation and leave it for the notification process. Krishnan then shared that the Prime Minister wants the pension reform bill passed and notified by August 15, so that he might reference it in his Independence Day Speech, as something accomplished, not just promised. The government did not view promises as adequate.

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Indian Commerce Minister Meets with USTR,
Others on WTO

¶5. (U) Media widely covered Commerce Minister Anand Sharma's first bilateral meetings with his counterparts, including USTR Ron Kirk, during the Cairns Group ministerial in Bali this week. Sharma, since taking charge as Commerce Minister in late May, has asserted India's commitment to conclude the WTO Doha Round, with an emphasis on the development aspects of the trade talks. At the Bali conference, Sharma emphasized that the "development dimension of the Doha round must be central to all discussions and the aspirations of all developing countries for a fair trading regime must be recognized." In addition to USTR Kirk and WTO Director General Lamy, the Indian minister also held talks with representatives from New Zealand, Australia, Malaysia and Indonesia, broadly highlighting the need to arrive at an early conclusion of the trade talks. Ahead of his departure for Indonesia, Sharma had reportedly said he hoped to re-start the process for the successful conclusion of the Doha Round and looked forward to his meeting with other trade ministers, especially USTR Kirk. Indian media reported there was considerable interest in the meetings Sharma had with other trade ministers, as India holds the key, along with the U.S., to the conclusion of the trade talks.

Tax Concessions Proposed for
Broadcast & Film Industry

¶6. (U) Press reported that the Ministry of Information & Broadcasting (MI&B) has recommended to the Ministry of Finance a "rationalization," i.e., lowering, of the tax/tariff structure on digital television set top boxes (STBs) and digital head-end equipment used by India's broadcasting and film industries. The proposals include: removal for five years of the current special additional 4% duty and the prevailing 8% duty on set top boxes in order to promote the conditional access system (CAS). MI&B also recommended that the Broadcasting, Cable, and Direct-to-Home (DTH) television industries be included in the "infrastructure sector," thereby granting to them the special benefits and incentives applicable to this sector. MI&B also recommended a 100% tax exemption on profits for digital cable service providers and DTH operators for the first five years. These proposals will be presented in the Parliament in early July during the budget session.

¶7. (SBU) Arvind Kumar, Director, MI&B confirmed to Post that these

recommendations have been submitted, noting the Ministry of Finance has authority to accept or reject any or all of them. The USG, through the U.S.-India Information and Communication Technology Working Group (ICT-WG), has been advocating tax rate reductions, implementation of CAS, and tighter regulation of the cable industry as a whole to stimulate consumer demand and to help reduce pirating of broadcasts.

Will Govt Give Bailout for Air India's Mounting Losses

¶8. (U) The government-owned National Aviation Company of India Ltd. (NACIL), the holding company for the merger of Air India and Indian Airlines, is facing mounting losses. NACIL has requested a bailout of \$2.8 billion from the central government in the form of equity infusion, soft loans, and grants. The bailout demand is higher than the carrier's actual operating revenue of \$2.4 billion in 2008-09. While NACIL's accounts for 2008-09 are still being finalized, losses are estimated to be around \$1 billion instead of the projected \$600 million at the beginning of the fiscal year. Given that this estimated loss is five times the combined losses of the two carriers before the merger in 2007, the merged entity continues to face criticism for underperforming and higher revenue losses. Industry observers have noted that part of the problem, amidst the global recession and downturn in aviation, is the large number of NACIL employees - including 33,000 direct hires and 20,000 contract employees - who have not been downsized to streamline costs of the merged entity. Press reports that NACIL has already used up a \$3.2 billion working capital loan facility; the company now faces the risk of lenders invoking the sovereign guarantee provided by the

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GOI.

¶9. (U) Civil Aviation Minister Praful Patel has recommended an initial public offer of NACIL's shares to help the airline get back on track. The public and aviation industry will also expect the ministry to impose tough pre-conditions on NACIL before approving such a hefty bailout. This may include a variety of measures to reduce costs, such as downsizing flights on unprofitable routes; reducing incentives, allowances, and placing a moratorium on wage escalation agreements for employees; returning leased planes; and minimizing the number of foreign pilots (which earn higher salaries than domestic pilots). However, despite the various problems facing NACIL, the company still plans to accept delivery of 111 new aircraft, of which 30 will be inducted this year. In contrast, private Indian carriers have withdrawn purchase orders and have deferred expansion plans. The aviation ministry will have to make a strong case for a government bailout of NACIL as well as outline measures to help NACIL turn around into a performing, profitable airline.

IT Industry Threatens Retaliation If US Tax Breaks Are Withdrawn

¶10. (U) President Som Mittal of the National Association of Software and Services Companies (NASSCOM) commented to media that any protectionist actions taken by the US that would adversely impact the outsourcing industry may trigger "counter-protectionist" measures by India. Mittal was referring to the Obama Administration's proposal to eliminate tax breaks that create incentives for U.S. companies to locate jobs overseas. Mittal did not elaborate on what "measures" would be taken, but estimated that ending tax incentives would affect approximately one million Indian IT professionals, a large portion of India's business process outsourcing (BPO) industry. The Indian IT industry has been closely monitoring President Obama's administration since the announcement of the proposal.

Chennai Breaks Ground on Metro Rail Project

¶11. (SBU) Chennai Metro Rail Limited began construction of a light rail link connecting northern Chennai to the city's international airport, southwest of town. The 23-kilometer rail project is officially slated for completion in 2015. Skeptics, however, have their doubts. An official at Chennai's Metropolitan Development Authority (which authorizes permits for buildings and other projects) told Consulate General Chennai that land acquisition for

the corridor continues to be problematic as much of the required land belongs to private owners in the city's central business district. He expects lengthy litigation to surround the acquisition process and that the project may run out of money as the acquisition process becomes more and more costly.

Local Distiller to Produce Smirnoff in Tamil Nadu

¶12. (SBU) International beverage giant Diageo has reached a deal with SNJ distilleries, a local bottler, to produce Smirnoff "Red" vodka for the local market, starting in September. Some Diageo products have been available at local "wine shops" (run by Tamil Nadu's state monopoly, known as TASMAC) since November 2008, but they have generally been too expensive to make much headway in the local market. The tie-up with a local distiller will allow Diageo to avoid paying the state's notoriously high import taxes and to therefore price "Red" more competitively. The marketing director for TASMAC told us that the new arrangement will allow Diageo to expand its customer base and revenue growth, emphasizing that TASMAC's customers are very price-conscious. (Comment: The owner of SNJ distilleries is politically well-connected, known to be a close friend of M.K. Stalin, Tamil Nadu's Deputy Chief Minister, who is also the son of Tamil Nadu's Chief Minister. While we do not have any direct information that these connections played a role in this venture, we suspect that they may have played a role in Diageo's decision. End Comment.)

¶13. (U) Visit New Delhi's Classified Website:

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<http://www.state.sgov/p/sa/newdelhi>.

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